



DEPARTMENT OF
FINANCE

ARNOLD SCHWARZENEGGER, GOVERNOR

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January 6, 2005

Assembly Member Nicole Parra, Chair
California State Legislature
Joint Legislative Audit Committee
1020 N Street, Room 107
Sacramento, CA 95814

Senator Wesley Chesbro, Chair
California State Senate
Budget and Fiscal Review Committee
State Capitol, Room 5019
Sacramento, CA 95814

Assembly Member John Laird, Chair
California State Assembly
Committee on Budget
State Capitol, Room 6026
Sacramento, CA 95814

Final Report—Review of Proposition 14 Bond Funds

In accordance with the Governor's directive, we respectfully submit the report on our review of the 2000 California Public Library Construction and Renovation Bond funds, as of June 30, 2003. The report includes a status of open bond projects, a review of project expenditures, findings, recommendations, and a response from the State Library. We plan to publish this report on the Department of Finance's website.

We appreciate the cooperation and assistance of Library staff and management with our review. If you have any questions, please contact me or Richard R. Sierra, Manager, at (916) 322-2985.

Sincerely,

Original Signed By:

Samuel E. Hull, Chief
Office of State Audits and Evaluations

Enclosure

cc: Ms. Susan Hildreth, State Librarian, California State Library (CSL)
Mr. Cameron D. Robertson, Deputy State Librarian, CSL
Mr. Andrew St. Mary, Bureau Chief, Administrative Services Bureau, CSL
Mr. Richard B. Hall, Bond Act Manager, Office of Library Construction, CSL
Mr. Curtis Purnell, Bond Act Fiscal Officer, Office of Library Construction, CSL
Office of the Legislative Analyst
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State Library, Governmental Publications Section

AR_{VIEW} OF B_{OND} F_{UNDS}

Proposition 14 California Public Library Construction and Renovation Fund Status of Bond Projects and Expenditures As of June 30, 2003

Prepared By:
Office of State Audits and Evaluations
Department of Finance

TABLE OF CONTENTS

Preface	iii
Executive Summary	iv
Introduction	1
Scope and Methodology	2
Project Overview and Status	4
Review of Bond Expenditures	10
Subsequent Events	12
Findings and Recommendations	13
Conclusion	17
Response	18

PREFACE

The Department of Finance, Office of State Audits and Evaluations, performed this review at the Governor's direction and under an interagency agreement with the California State Library, Office of Library Construction (OLC). The review's purpose was to determine the project status of the California Reading and Literacy Improvement and Public Library Construction and Renovation Bond Act of 2000 (Proposition 14) funds, and to audit the expenditures of these funds for the period July 1, 2000 through June 30, 2003. Specifically, our objectives were to:

- Obtain from the OLC information on the status of Proposition 14 bond projects, including projects approved, expenditures incurred, and remaining appropriation balance.
- Review the OLC's internal control to determine areas of risk and to identify where the control and accountability for bond funds could be improved.
- Audit a sample of bond program expenditures for the period July 1, 2000 through June 30, 2003 for accuracy and fiscal compliance with statutory or contractual requirements. Expenditures include state operations and local assistance.

This report includes audit results for fiscal years 2000-01 through 2002-03, and summarizes cumulative information since program inception.

We did not conduct a performance review to assess the effectiveness and efficiency of the bond program's operations or program compliance. The scope of our review was limited to fiscal compliance.

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EXECUTIVE SUMMARY

During our review of the California Reading and Literacy Improvement and Public Library Construction and Renovation Bond Act (Proposition 14) funds for the period July 1, 2000 through June 30, 2003, we determined that, except as noted, the bond funds and bond-acquired assets were accurately accounted and reported in compliance with the bond act, and in conformity with the accounting practices prescribed by the State of California. The following is a summary of our findings:

As of June 30, 2003:

- Cumulative expenditures, encumbrances, and other commitments totaled \$164,947,505
- \$185,052,495 of the total appropriation remained unexpended, unencumbered, and uncommitted.
- There were 18 approved projects.

Internal Control Issues

As discussed in the *Findings and Recommendations* section of this report, we identified areas where the control and accountability for the bond funds could be strengthened, and have provided recommendations to improve fiscal operations. The control issues pertain to accounting, reporting, and monitoring.

Background

In March 2000, California voters passed a bond measure enacting the California Reading and Literacy Improvement and Public Library Construction and Renovation Bond Act (Proposition 14). Implemented by Chapter 726, Statutes of 1999 (Education Code section 19987), and administered by the California State Library, Office of Library Construction (OLC), the proceeds from these bonds support the acquisition or construction of new public library facilities or additions to existing libraries. The OLC Board authorizes the disbursement of bond proceeds to local agencies via grants, and these agencies expend the funds on OLC-approved construction projects. Program requirements are codified in Title 5 and Title 24 of the California Code of Regulations.

To finance these costs, the bond program provides for the issuance and sale of \$350 million in general obligation bonds of the State of California, and the establishment of the California Public Library Construction and Renovation Fund, for depositing the bond proceeds and carrying out the purposes specified in the act. Operating cash is provided by short-term loans from the State's Pooled Money Investment Account (PMIA). The PMIA loans are repaid upon the sale of bonds.

SCOPE AND METHODOLOGY

On November 9, 1999, the Governor directed the State agency administering Proposition 14 funds “to annually report to the Department of Finance: a list of projects approved, the progress of the project or actual expenditures made, and the amount of funds remaining in each account.” The Governor also directed the Department of Finance to annually audit and report on the expenditure of these funds.

In response to the Governor’s directive, the Department of Finance, Office of State Audits and Evaluations, has completed its audit of Proposition 14 expenditures as of June 30, 2003, and presents its first annual report.

Our scope included an audit of the Proposition 14 bond controls and transactions for the period July 1, 2000 through June 30, 2003, and a compilation of OLC-reported project information as of June 30, 2004, with the objective of determining whether the bond expenditures and encumbrances were accurately reported. The methods used and procedures performed by scope area are as follows:

- **We determined whether the OLC had effective control and accountability for bond funds, and whether it had adequate project monitoring processes.** For this area, we interviewed the OLC’s fiscal and program staff, observed operations and activities, reviewed policies and procedures, reviewed contract terms and project scopes, reviewed project files for evidence of periodic monitoring and submission of required documentation, and tested a sample of bond expenditures for proper authorization and compliance with established procedures. We found that, except as noted, bond funds and bond-acquired assets were safeguarded against loss from unauthorized use or disposition, and bond transactions were executed in accordance with management’s authorization and recorded properly to permit the preparation of reliable financial reports. Identified program monitoring weaknesses are described in the *Findings and Recommendations* section of this report.
- **We determined whether bond funds were expended and reported in accordance with the bond act and State accounting requirements.** To complete this objective, we reviewed the bond act and applicable laws and regulations, reviewed policies and procedures, interviewed the OLC’s management and staff, reviewed and verified bond allocations and appropriations, verified fund transfers, reconciled accounting records with financial reports, tested a sample of expenditures (support and local assistance) to supporting documents, reviewed grant agreements and contracts, and verified the validity of encumbrances and reserves. We found that, except as noted, the bond expenditures for the period July 1, 2000 through June 30, 2003, were accurately accounted and reported in compliance with the bond act, and in conformity with the accounting practices as prescribed by the State of California.

The results of our audit are summarized on pages 10-11. Identified accounting and reporting weaknesses are described in the *Findings and Recommendations* section of this report.

- **We determined whether the OLC's self-reported project status appeared complete, consistent, and informative.** In accordance with the Governor's directive, we requested the OLC to report to us the status of its open projects. The results are summarized in the *Project Overview and Status* section of this report. The project status information was reported to us through June 30, 2004. Because this information is estimated and self-reported, our auditing procedures did not extend to a verification of the expected completion dates, and we make no representations about their accuracy. However, we reviewed the information for consistency and completeness and followed up with the OLC to clarify and specify details. We will continue reviewing project completion during subsequent field audits of grantees.

Our review did not include an assessment of the bond authorization, issuance, and sale processes, or an examination of the efficiency or effectiveness of program operations.

PROJECT OVERVIEW AND STATUS

Since program inception in July 2000, the Office of Library Construction (OLC) has developed processes to review applications, identify and prioritize projects and grantees, and administer the bond program. Project grants are available on a 65 percent State to 35 percent local matching fund basis to cities, counties, and library districts authorized to own and maintain a public library facility. The OLC Board awards grants in three cycles. As of June 30, 2003, Cycle One grants had been awarded to 18 local agencies. In order to report the most current information available, the OLC provided the following project overview and status as of June 30, 2004, which includes an additional 16 Cycle Two grants awarded after June 30, 2003. The OLC plans to award Cycle Three grants during fiscal year 2004-05. We performed limited tests of the information provided, some of which was obtained from the OLC's website.

The entire \$350 million Proposition 14 allocation has been appropriated and is available for expenditure. As of June 30, 2004, the OLC awarded 34 projects totaling \$257,383,961. The awards, which range from \$500 thousand to \$20 million, were made through the first two award cycles. The 18 Cycle One awards totaled \$149,226,329, of which \$2,355,755 had been disbursed to local agencies as of June 30, 2003. The 16 Cycle Two awards totaled \$108,157,632, of which no funds had been disbursed as of June 30, 2003 (date through which our expenditure tests were conducted). The OLC anticipates that most library projects will be completed by fiscal year 2011-12.

The following is a summary of the 34 approved projects:

Cycle One Awards

New Camarillo Library: The city of Camarillo plans to construct a new library beginning in April 2004. Centrally located within the city, the 65,621 square foot library will be a joint venture facility, serving city and Ventura County residents, as well as Pleasant Valley School District students. Total project costs are budgeted at \$24.5 million, including \$15.6 million of Proposition 14 funds. The estimated completion date is July 2005. As of June 30, 2004, the library's schematic design and design development plans had been accepted.

Note: A joint venture facility serves both public library users and any combination of K-12 students, as defined by a cooperative agreement between a public library jurisdiction and one or more public school districts.

Alameda Free Library: Beginning in March 2004, the city of Alameda plans to construct a new 47,470 square foot downtown library. The library will be a joint venture facility, serving both city residents and Alameda School District students. Total project costs are budgeted at \$24 million, including \$15.5 million of Proposition 14 funds. The estimated completion date is April 2005. As of June 30, 2004, the city had opened construction bids for the project.

San Mateo Public Library: The city of San Mateo plans to construct a new main library beginning in February 2004. The 93,800 square foot facility, to be located at the same downtown site as the old library, will be a joint venture facility, serving city residents and San Mateo/Foster City School District students. Total project costs are budgeted at \$61.4 million, of which \$20 million is from Proposition 14. The estimated completion date is November 2005. As of June 30, 2004, the city had opened construction bids for the project.

Hercules Public Library: The city of Hercules plans to construct a new library starting in February 2004. The 20,492 square foot library will be a joint venture facility, serving city and Contra Costa County residents, as well as West Contra Costa Unified School District students. Total project costs are budgeted at \$10.1 million, including \$6.2 million of Proposition 14 funds. The estimated completion date is March 2005. As of June 30, 2004, the library's design development plans had been accepted.

Highland Branch Library: The city of Highlands plans to construct a new library starting in March 2003. The library will be part of a 30-acre multi-purpose complex. At 30,016 square feet, the library will be a joint venture facility, serving city and San Bernardino County residents, as well as San Bernardino City Unified School District students. The Cypress Elementary School library will also be located in the new facility. Total project costs are budgeted at \$8.2 million, including a Proposition 14-funded portion of \$5.2 million. The March 2004 estimated completion date requires revision. As of June 30, 2004, the library's design development plans had been accepted.

South Oxnard Branch Library: The city of Oxnard plans to construct a new branch library beginning in September 2004. The library will be located adjacent to the South Oxnard Community Center, which houses a senior center and a childcare center. The 23,000 square foot library will be a joint venture facility, serving city residents and Ocean View/Hueneme School District students. Total project costs are budgeted at \$9.7 million, of which \$5.8 million is funded from Proposition 14. The estimated completion date is January 2006. As of June 30, 2004, the library's design development and construction plans had been accepted.

Manor Community Branch Library: The city of San Leandro plans to construct a new branch library starting in July 2003. The 9,500 square foot library will be located at the same site as the existing branch, and will be a joint venture facility, serving city residents and San Leandro Unified School District students. Total project costs are budgeted at \$5.9 million, of which \$3.8 million is funded from Proposition 14. Through June 2003, the city had expended \$587,340 on the project. The estimated completion date will need to be revised from the original May 2004 estimate. As of June 30, 2004, construction bids had been opened.

National City Public Library: National City plans to construct a new, centrally-located library beginning in October 2003. The 48,998 square foot library will be a joint venture facility, serving city residents and National School District students. Total project costs are budgeted at \$17.4 million, including a Proposition 14 funded portion of \$11.1 million. The estimated completion date is February 2005. As of June 30, 2004, construction had begun.

Victoria Gardens Library: The city of Rancho Cucamonga plans to construct a new multipurpose facility beginning in September 2003. Located in the Victoria Gardens Regional Mall, the facility will include a library, children's theatre, and event center. The library will occupy 26,863 square feet and will be a joint venture facility, serving city residents and Etiwanda School District students. Total project costs are budgeted at \$13.7 million, of which

\$7.8 million is funded from Proposition 14. The estimated completion date is January 2005. As of June 30, 2004, construction had begun on the multipurpose facility.

Lemon Grove Public Library: The city of Lemon Grove plans to construct a new multipurpose facility commencing in April 2004. Located in the Civic Center Complex, the facility will include a library, conference center, and educational center. The 18,564 square foot library will be a joint venture facility, serving city and San Diego County residents, as well as Lemon Grove School District students. Total project costs are budgeted at \$6 million, including \$3.8 million funded from Proposition 14. The estimated completion date is October 2005. As of June 30, 2004, the city had finalized its grant agreement with the OLC. On November 18, 2004, the city of Lemon Grove notified the OLC that due to the city's inability to obtain the required matching funds, it will not utilize the grant award, and intends to return any outstanding funds to the OLC.

Mariners Joint Use Library: Beginning in September 2003, the city of Newport Beach plans to construct a 15,125 square foot branch library adjacent to Mariners Park. The Mariners Elementary School's library will be co-located within the city's library. Total project costs are budgeted at \$5.1 million, of which \$3.2 million is funded from Proposition 14. The September 2004 estimated completion date requires revision. As of June 30, 2004, the library's design development plans and construction documents had been accepted.

Orange Main Library Expansion: The city of Orange plans to remodel and expand its main library in January 2005. The existing library, built in 1961, will be expanded from 17,000 to 45,000 square feet. Total project costs are budgeted at \$16.5 million, including a Proposition 14 funded portion of \$9.1 million. The city had expended \$617,000 through June 2003. The estimated completion date is July 2006. As of June 30, 2004, the library's design development plans and construction documents had been accepted.

Bruggemeyer Memorial Library: The city of Monterey Park plans to remodel and expand its library in February 2004. The existing library was last renovated in 1979, and will be expanded from 26,354 to 53,237 square feet. Total project costs are budgeted at \$13.9 million, of which \$8.9 million is funded from Proposition 14. The city has expended \$647,000 through June 2003. The estimated completion date is February 2005. As of June 30, 2004, construction bids had been opened.

Santa Maria Public Library: The city of Santa Maria plans to construct a new Civic Center library beginning in November 2003. The 60,825 square foot library will be a joint venture facility, serving both city residents and Santa Maria Joint Union High School District students. Total project costs are budgeted at \$25.3 million, of which \$16.4 million is funded from Proposition 14. The estimated completion date is September 2005. As of June 30, 2004, the library's schematic design had been accepted.

Julian Branch Public Library: The county of San Diego constructed a new branch library in the rural, historic town of Julian. The 9,573 square foot library is a joint venture facility, serving county residents and Julian Union School and High School District students. The \$3.9 million project included \$2.5 million in Proposition 14 funds. The library opened to the public on September 14, 2004.

Haskett Branch Library: Beginning in January, 2004, the city of Anaheim plans to replace its existing Maxwell Park branch library. The new 24,000 square foot library will be a joint venture facility, serving city residents, Maxwell Elementary School, and Magnolia School District

students. Total project costs are budgeted at \$8.7 million, of which \$5.7 million is funded from Proposition 14. The city has expended \$504,000 through June 2003. The estimated completion date is December 2004. As of June 30, 2004, the library's design development plans and construction documents had been accepted.

Logan Heights Public Library: Beginning in September 2003, the city of San Diego plans to construct a new branch library in the Memorial Park area, near several elementary schools. The 25,000 square foot library will be a joint venture facility, serving city residents and San Diego Unified School District students. Total project costs are budgeted at \$8.8 million, with a Proposition 14 funded portion of \$5.4 million. The September 2004 estimated completion date requires revision. As of June 30, 2004, the library's construction documents had been accepted.

Visalia Library Remodel and Expansion: The county of Tulare plans to remodel and expand its Visalia branch library in June 2004. The existing 42,970 square foot library, last renovated in 1976, will be expanded to 45,192 square feet. Total project costs are budgeted at \$5.3 million, of which \$3.4 million is funded from Proposition 14. The estimated completion date is April 2005. As of June 30, 2004, the library's schematic design had been accepted.

Cycle Two Awards

Pickleweed Library: The city of San Rafael plans to remodel and expand its Pickleweed Library beginning in September 2004. The library is part of the multi-use Pickleweed Park Community Center. The existing library will be expanded from 526 to 6,487 square feet. Total project costs are budgeted at \$2 million, including \$1.3 million funded from Proposition 14. The estimated completion date is September 2005. As of June 30, 2004, the library's schematic design had been accepted.

Redding Main Library: Beginning in January 2005, the county of Shasta plans to build a new main library in the city of Redding, adjacent to City Hall and near the downtown area. The 55,000 square foot library will be a joint venture facility, serving the city of Redding, Shasta County, Shasta Union High School District, and Redding School District. Total project costs are budgeted at \$20 million, of which \$12.2 million is funded from Proposition 14. The estimated completion date is April 2006. As of June 30, 2004, the library's schematic design and design development plans had been accepted.

Castroville Library: Beginning in April 2003, the county of Monterey plans to build a new branch library near downtown Castroville. The 9,163 square foot library will be a joint venture facility, serving the city of Castroville, Monterey County, and North Monterey County School District. Total project costs are budgeted at \$5.3 million, with a Proposition 14 funded portion of \$3.2 million. The completion date will need to be revised from its original March 2004 estimate. As of June 30, 2004, the library's schematic design and design development plans had been accepted.

MacArthur Park Library: The city of Long Beach plans to build a new MacArthur Park branch library in February 2005. The 16,155 square foot library will be a joint venture facility, serving city residents and Long Beach Unified School District students. Total project costs are budgeted at \$10.1 million, including \$6.4 million in Proposition 14 funds. The estimated completion date is April 2006. As of June 30, 2004, the city had finalized its grant agreement with the OLC.

Frazier Park Library: Beginning in February 2005, the county of Kern plans to build a new branch library in the community of Frazier Park. The 9,972 square foot library will be a joint venture facility, serving county residents and El Tejon Unified School District students. Total project costs are budgeted at \$5.6 million, of which \$3.4 million is funded from Proposition 14. The estimated completion date is March 2006. As of June 30, 2004, the county had finalized its grant agreement with the OLC.

Mendota Library: Beginning in June 2004, the county of Fresno plans to build a new Mendota branch library adjacent to Mendota High School. The 12,635 square foot library will be a joint venture facility, serving city and county residents, and Mendota Unified School District students. Total project costs are budgeted at \$5.6 million, including \$3.5 million funded from Proposition 14. The estimated completion date is June 2005. As of June 30, 2004, the county had finalized its grant agreement with the OLC.

Hesperia Library: In April 2005, the city of Hesperia plans to build a new library adjacent to the proposed Hesperia Government Center. The 20,000 square foot library will be a joint venture facility, serving both city and San Bernardino County residents, and Hesperia Unified School District students. Total project costs are budgeted at \$6.8 million, of which \$4.2 million is funded from Proposition 14. The estimated completion date is April 2006. As of June 30, 2004, the library's schematic design had been accepted.

Dorris Library: The city of Dorris plans to build a new library beginning in May 2004, in close proximity to the city's schools and medical clinic. The 3,300 square foot library will be a joint venture facility, serving city and Siskiyou County residents, and Butte Valley Unified School District students. Total project costs are budgeted at \$895,000, of which \$534,000 is funded from Proposition 14. The December 2004 estimated completion date may require revision. As of June 30, 2004, the library's schematic design and design development plans had been accepted.

Harbor-Gateway Library: The city of Los Angeles plans to build a new Harbor Gateway/Harbor City branch library in July 2004. The 14,621 square foot library will be a joint venture facility, serving Harbor City residents and Los Angeles Unified School District students. Total project costs are budgeted at \$9.7 million, including \$5.7 million funded from Proposition 14. The estimated completion date is October 2005. As of June 30, 2004, construction bids had been opened.

Calabasas Library: Beginning in December 2004, the city of Calabasas plans to build a new library in the city's Civic Center Complex. The 23,332 square foot library will be a joint venture facility, serving city residents and Las Virgenes Unified School District students. Total project costs are budgeted at \$18.6 million, of which \$8.2 million is funded from Proposition 14. The estimated completion date is May 2006. As of June 30, 2004, the city had finalized its grant agreement with the OLC.

Temecula Library: The city of Temecula plans to build a new library beginning in June 2004, in close proximity to several schools, the Rancho California Sports Park, and the Community Recreation Center. The 34,000 square foot library will be a joint venture facility, serving city and Riverside County residents, as well as Temecula Valley Unified School District students. Total project costs are budgeted at \$15 million, including \$8.5 million in Proposition 14 funds. The estimated completion date is December 2005. As of June 30, 2004, the library's construction documents had been accepted.

San Diego Main Library: Beginning in September 2004, the city of San Diego plans to build a new main library at the Park-to-Bay site, within the city's central business district. The 286,327 square foot library will be a joint venture facility, serving city residents and San Diego Unified School District students. Total library project costs are budgeted at \$159.1 million, including \$20 million funded from Proposition 14. The estimated completion date is December 2006. As of June 30, 2004, the city had finalized its grant agreement with the OLC.

Redwood Shores Library: Beginning in December 2005, Redwood City plans to build a new branch library in the Redwood Shores community. The 22,558 square foot library will be a joint venture facility, serving city residents and Sequoia Union School District and Belmont/Redwood Shores School District students. Total project costs are budgeted at \$17 million, of which \$10.1 million is funded from Proposition 14. The estimated completion date is April 2007. As of June 30, 2004, the city had finalized its grant agreement with the OLC.

Fairfield-Cordelia Library: Beginning in September 2004, the city of Fairfield plans to build a new library in the community of Cordelia. The 16,459 square foot library will be a joint venture facility, serving city and Solano County residents, along with Fairfield-Suisun Unified School District students. Total library project costs are budgeted at \$12 million, with a Proposition 14 funded portion of \$4.1 million. The estimated completion date is September 2005. As of June 30, 2004, the city had finalized its grant agreement with the OLC.

Lincoln Library: The city of Lincoln plans to build a new library in December 2004, co-located in the same complex with a Western Placer Unified School District library and a Sierra Community College library. The 37,872 square foot library will be a joint use facility, serving the city, Western Placer Unified School District, and Sierra Community College District. Total project costs are budgeted at \$16.4 million, of which \$10.4 million is funded from Proposition 14. The estimated completion date is March 2006. As of June 30, 2004, the city had finalized its grant agreement with the OLC.

Murrieta Library: The city of Murrieta plans to build its first permanent library in August 2004, adjacent to the historic downtown area and centrally located near public schools. The 24,951 square foot library will be a joint venture facility, serving city residents and Murrieta Valley Unified School District students. Total project costs are budgeted at \$10 million, with \$6.4 million funded from Proposition 14. The estimated completion date is August 2005. As of June 30, 2004, the library's schematic design had been accepted.

REVIEW OF BOND EXPENDITURES

The information presented on the accompanying schedule was prepared from the accounts and financial transactions of the California State Library, Office of Library Construction (OLC), and in accordance with the legal/budgetary basis of accounting prescribed by the State of California, which is a comprehensive basis of accounting other than generally accepted accounting principles. Under this method, spending authority is created by legislative appropriation, and expenditures are recorded when obligations for goods and services are incurred. We audited the financial information for accuracy, reasonableness, classification, and presentation, and adjusted the schedule for any material errors, exceptions, or misstatements. The information presented is for the period July 1, 2000 through June 30, 2003.

**California State Library
Office of Library Construction**

**California Public Library Construction and Renovation Fund
Schedule of Appropriations, Expenditures, Encumbrances, and Reserves
For the Period July 1, 2000 through June 30, 2003**

Appropriations:

Chapter 726, Statutes of 1999 ¹	<u>\$350,000,000</u>
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Deductions:

Expenditures ²	8,655,339
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Encumbrances ²	134,902,409
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Reserve for Commitments ³	8,785,855
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Reserve for Statewide Costs and Future Obligations ⁴	<u>12,603,902</u>
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Total Deductions	<u>164,947,505</u>
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Available Appropriation Balance, June 30, 2003⁵	<u>\$185,052,495</u>
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¹Proposition 14 funds were continuously appropriated beginning with fiscal year 2000-01.

²Expenditures and encumbrances are shown net of any adjustments.

³Reserve for commitments includes funds awarded for specific projects, where contracts have been initiated but not yet executed.

⁴Amount represents the OLC's estimated program delivery, financing, and support costs during the life of the program.

⁵As of June 30, 2003, this amount had not yet been awarded for specific projects or otherwise reserved for future program costs.

SUBSEQUENT EVENTS

Cycle Two Awards: As of October 28, 2003, the OLC Board awarded 16 Cycle Two grants, totaling \$108,157,632. Contracts were executed during the period December 2003 through August 2004. Information on these awards is included in the *Project Overview and Status* section of this report.

Cycle Three Awards: As of April 28, 2004, the OLC received 72 Cycle Three applications and determined that all were eligible for bond funding. The OLC is now evaluating each application to determine priority. The OLC Board plans to meet during Fall 2004 to make award decisions for the remaining bond funds.

Proposed Legislation: In September 2004, Governor Schwarzenegger signed Senate Bill 1161, the California Reading and Literacy Improvement and Public Library Construction and Renovation Bond Act of 2006, authorizing \$600 million of State general obligation bonds to be placed on the March 2006 ballot. These bonds will finance the construction and improvement of public library facilities. If approved, the act would provide priority funding of up to \$300 million for eligible, unfunded third cycle applications from the current Proposition 14 program. The remaining \$300 million would be available to local jurisdictions through a statewide application process. The potential fiscal impact on the Proposition 14 program is not yet known.

FINDINGS AND RECOMMENDATIONS

In planning and performing our audit of Proposition 14 expenditures, we reviewed the applicable internal control of the OLC to determine areas of risk and to identify where the control and accountability for bond funds could be improved. In general, we found that bond funds and bond-acquired assets were adequately accounted, safeguarded, and reported in compliance with the bond act and State fiscal requirements. However, we noted certain conditions that require corrective action to improve fiscal operations. The following conditions illustrate the importance of designing controls that enhance the OLC's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

FINDING 1 Administrative Oversight Could Be Improved

Conditions: We identified a number of weaknesses in the OLC's fiscal and project management controls that may expose bond funds to misuse, errors, and irregularities. The weaknesses pertain to inconsistent or inadequate review and monitoring of program expenditures and projects.

- A. Fiscal Monitoring. The OLC does not have sufficient internal procedures to ensure that bond expenditures are accurately recorded and reported. The OLC currently relies on monthly Calstars reports obtained from Contracted Fiscal Services (CFS), but does not regularly review these reports or reconcile them with other internal documents for completeness and accuracy. As discussed in Finding 2 below, we found a number of fiscal errors and omissions that may have been detected sooner, had the OLC reviewed the reports. Without a consistent review process, unauthorized expenditures could be charged to the bond funds and grant awards could exceed the appropriation balance. We are not suggesting that the OLC duplicate work performed by CFS, but are recommending that the OLC check the monthly reports for accuracy.
- B. Project Monitoring. The OLC does not adequately monitor grant awards and projects to ensure that bond funds are used only for authorized purposes, and that actual projects are progressing in accordance with award agreements. Although the OLC conducts a rigorous pre-award review and approval process, there is almost no follow-up with grantees after funds are disbursed. Project files contain insufficient information on project progress and status. The OLC does not require grantees to submit periodic progress reports, other than the limited information included with payment requests. Payment requests are subject to only a cursory review

of budget compliance. In addition, there was no evidence that OLC staff made site visits to validate project progress, performance, and costs.

Although our fiscal audits will help mitigate some of the monitoring risks, because the audits are done in arrears after expenditures have been incurred and work completed, they may not accomplish the OLC's need for more proactive and contemporaneous oversight.

We recognize that OLC staffing levels may preclude regular site visits and inspections, but there are prudent, cost-effective steps the OLC can take with existing resources, as described in the recommendations.

Criteria: Education Code section 19992 charges the State Librarian with administration of the Proposition 14 funds. The Office of Library Construction was created within the State Library to administer the funds, including fiscal and program oversight.

Government Code section 13403 states that the elements of a satisfactory system of internal accounting and administrative control shall include, but are not limited to, a system of authorization and record keeping procedures adequate to provide effective accounting control over assets, liabilities, revenues, and expenditures; and an effective system of internal review.

- Recommendations:
- A. Establish procedures to monitor bond funds, including, but not limited to, the following activities:
 - 1. Review Calstars expenditure reports monthly for completeness and accuracy.
 - 2. Reconcile Calstars reports to internal expenditure records monthly. If necessary, develop a reconciliation form for this purpose.
 - 3. Regularly monitor the appropriation balance and ensure that awards and projected expenditures do not exceed the available appropriation.
 - 4. Review year-end financial statements to ensure that bond activity and account balances are accurately reported.
 - 5. Document the above activities and retain for audit.
 - B. Establish procedures to monitor bond projects, including, but not limited to, the following activities:
 - 1. Require grantees to submit quarterly progress reports to the OLC. The reports should contain sufficient information for the OLC to determine if the project is proceeding in accordance with the grant award, such as the following:
 - a. Percentage of completion
 - b. Major accomplishments to date

- c. Expenditures to date
 - d. Estimated completion date
 - e. Significant problems, delays, disputes
 - f. Evidence of inspection by grantee's construction manager, certifying adequate completion of work
 - g. Grantee certification that project expenditures and activities are in compliance with program requirements
 - h. Project photographs
2. Review the quarterly status reports and follow-up on reported items as necessary.
 3. Perform site visits of significant and/or troubled projects to monitor activities, ensure program compliance, and discuss problem resolution (if any).
 4. Issue information bulletins or other communications to grantees clarifying compliance and fiscal reporting requirements.
 5. Document the above activities and retain for audit.

FINDING 2

Accounting and Reporting Errors

We identified the following conditions impacting the OLC's ability to accurately record transactions and prepare reliable financial statements. Although conditions B through D were primarily offsetting, their occurrence highlights unaddressed weaknesses in fiscal controls that, if left uncorrected, could lead to material misstatement. Condition A is a material weakness.

Conditions:

- A. **Grants Not Encumbered.** As of June 30, 2003, the OLC did not encumber sixteen bond grants totaling \$134,885,108, for which valid agreements existed at year-end. Because the encumbrances were not made, there was no identification of amounts that should be accrued and recorded as expenditures in the year-end financial statements. The schedule on page 11 has been adjusted to reflect these encumbrances.
- B. **Improperly Accrued Contract.** Due to an improper contract accrual, the OLC overstated its fiscal year 2002-03 accounts payables and expenditures by \$450,000. The specific contract was not executed until October 28, 2003, and no expenditures were incurred for the fiscal year ended June 30, 2003.
- C. **Understated Salaries and Benefits.** Due to a position coding error, \$238,000 in Proposition 14 salaries and benefits were improperly charged to another fund, resulting in the understatement of expenditures for fiscal years 2000-01 through 2002-03. The OLC's approved Budget Change Proposal specifically identified this position as Proposition 14 funded. The OLC subsequently corrected the error in fiscal year 2003-04.

- D. Net Interest Expense Not Estimated. The OLC did not include \$229,123 of net interest expense in its estimated administrative costs. Without the inclusion of interest expense in its projections, the OLC cannot ensure that there will be sufficient funds to pay for future costs, or that the uncommitted fund balance accurately reflects the available program funds.

Criteria: Government Code section 13403 states that the elements of a satisfactory system of internal accounting and administrative control shall include, but are not limited to, a system of authorization and record keeping procedures adequate to provide effective accounting control over assets, liabilities, revenues, and expenditures.

State Administrative Manual (SAM) section 10608 requires that encumbrances be established for valid obligations, and that accounts payable be accrued at June 30 for the portion of the obligation that will result in actual expenditures for the year then ended.

- Recommendations:
- A. Encumber grant awards upon execution of grant agreements.
 - B. Accrue only valid accounts payable at June 30, for which goods and services are received and actual expenditures incurred. Review the year-end report of accruals for accuracy and completeness.
 - C. Review all expenditures monthly to ensure that authorized bond expenditures are recorded in the proper fund and account.
 - D. Include net interest expense in the estimated administrative costs.

FINDING 3 Lack of Cost Allocation Plan

Condition: The California State Library does not have a current cost allocation plan to equitably allocate administrative costs to all of its programs and funding sources, including Proposition 14. For fiscal years 2000-01 through 2002-03, we identified several instances where allocated costs were either not supported, or not reasonably allocated between the OLC and other programs. Although the questionable costs were offsetting and not material, without a current, approved cost allocation plan, there is an increased risk that the Proposition 14 program could pay expenses significantly in excess of the actual costs of administering the program.

Criteria: SAM section 9202 requires all state agencies to document their cost allocation procedures and methods in a Cost Allocation Plan (CAP). Each CAP will contain detailed, documented information regarding the costs being allocated, the allocation method/basis, justification for the selected method, and provisions for periodic review and revision.

Recommendation: Develop a cost allocation plan to equitably distribute administrative costs to all programs and funding sources. Retain documentation of the plan, and periodically adjust the plan and accounting records as necessary.

CONCLUSION

We respectfully submit this report on our review of the California Public Library Construction and Renovation Bond Act (Proposition 14) funds as of June 30, 2003.

The control and accountability issues discussed in the *Findings and Recommendations* section present opportunities to correct identified weaknesses and improve operations. We believe the internal control would be strengthened if the OLC implements our recommendations. The internal control weaknesses, if left uncorrected, increase the risk that material errors or irregularities could occur and remain undetected.

Except as discussed in the following paragraph, we conducted our review in accordance with *Government Auditing Standards* (GAS), issued by the Comptroller General of the United States, based on fieldwork performed from January 7, 2004 to September 14, 2004. We limited our review to those areas specified in the scope section of this report.

In connection with our review, there are certain disclosures required by GAS Statement No. 3. Both the OLC and the Department of Finance, of which the Office of State Audits and Evaluations is a unit, are part of the Executive Branch, which GAS considers an impairment to independence. Also, as required by various statutes within the California Government Code, the Department of Finance's other units are mandated to perform certain management and accounting functions. These activities impair independence. Although the Department of Finance is statutorily obligated to perform these specific activities, we believe that sufficient safeguards and divisions of responsibility exist that would enable the reader of this report to rely on the information contained herein.

Original Signed By:

Samuel E. Hull, CPA
Chief, Office of State Audits and Evaluations
(916) 322-2985

September 14, 2004



CALIFORNIA
STATE LIBRARY
FOUNDED 1850

December 10, 2004

Mr. Samuel E. Hull
Department of Finance
300 Capitol Mall, Suite 801
Sacramento, CA 95814

Dear Mr. Hull:

Thank you for the opportunity to respond to the draft audit report of the California Reading and Literacy Improvement and Public Library Construction and Renovation Bond Act of 2000. We appreciate the efforts of the auditors working with the California State Library, which administers this bond program, and the cooperative and responsive relationships that have developed.

This is the initial audit of this program and it has been helpful and informative. Since we are a small agency your staff's expertise in these areas is most welcome. Now that the application phase of the program is over, November 29, 2004, the Office of Library Construction will be able to reallocate existing staff resources to a much more focused effort on the monitoring and administrative functions of the program. The audit and this change in phases of the program are well timed because the cycle one projects are now reaching construction stages, which is where the majority of the funds will be expended. The staff will be working on the findings and recommendations with all appropriate parties. It is gratifying to note that this initial audit of the program confirmed that bond funds were accurately accounted for and reported in compliance with the bond act, and in conformity with the accounting practices prescribed by the State of California.

We look forward to our continued working relationship with the Department of Finance staff.

Yours truly,

Original Signed By:

Cameron D. Robertson
Deputy State Librarian of California

CDR:cpt